

Ernst Fraenkel Vorträge

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Politik, Wirtschaft, Gesellschaft und Geschichte

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James S. Coleman

Parents' Rights in Choice of School

David O. Sears

**Ethnic Conflict and the Politics of Race
in the United States**

Rachel McCulloch

The Impact of Foreign Ownership on U. S. Business

John F. Kennedy-Institut für Nordamerikastudien
der Freien Universität Berlin

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Editor's Preface

This series published by the John F. Kennedy Institute of the Free University of Berlin aims at preserving in a longer perspective the results of the Ernst Fraenkel lectures on American politics, economy, society and history and making them accessible to a broad public outside of Berlin as well. These lectures are dedicated to Ernst Fraenkel, himself a German-American and an internationally renowned political scientist and expert on American affairs, who taught at the Free University from 1951 to 1967 and whose initiative led to the founding in 1963 of the John F. Kennedy Institute for North American Studies. As was the case with Ernst Fraenkel's life and work, these lectures held by eminent American scholars and authorities of some particular field are meant to contribute to forging an academic link across the Atlantic and to provide stimulation for research at the Kennedy Institute as well as at other European institutes for North American studies.

This issue contains lectures delivered at the Kennedy Institute during the winter semester 1991/92 by three prominent American scholars on current political, social, and economic issues in the United States.

On November 6, 1991, the sociologist James S. Coleman (University of Chicago), the main author of the famous *Coleman Report* of 1966 on the equality of educational opportunity, presented his lecture on an important issue in the current discussions on the improvement of education in American schools, namely the rights of parents to choice of school. Should the public school system be made more competitive in order to improve its quality? Should parents be allowed to choose any public school for their children independently of their residential area, as they can already do when they select a private school? Coleman provides a theoretical background to the issue and comes up with surprising implications and results.

On November 27, 1991, the political scientist David O. Sears (University of California at Los Angeles) lectured on the latest stage of racism in the United States, namely "symbolic racism", which ties together simple racism of the traditional type and attitudes based on non-racial ideologies, beliefs, or values that in effect lead to a discrimination of blacks or other ethnic minorities. The concept is used to interpret events, such as the police beating of Rodney King in Los Angeles, which were given prominent play in the media with a view to their significance in race relations. The paper serves as a survey of the latest state of research on the topic.

Finally, on January 16, 1992, the economist Rachel McCulloch (Brandeis University and National Bureau of Economic Research) presented her insights into the causes of the recent and rapid rise of foreign direct investment in the United States and its impact on U.S. business, economic performance in general, and economic policy in particular.

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Parents' Rights in Choice of School

James S. Coleman

Probably the strongest policy debate in American education today concerns the issues of parents' choice of school. The debate concerns a cluster of issues, because several different things are meant by "parents' choice of school." At one extreme is choice that erases the financial barrier to use of private schools through providing vouchers that can be used to cover all or most tuition costs of private school. At the other extreme is merely increased approval of requests for transfers from the school to which a child has been assigned. In between there is a variety of possibilities. In Minnesota, for example, the state has legislation which allows free choice between schools in different school districts. This choice cannot be refused by the district or school from which the child is leaving (except that a district under a racial desegregation court order may refuse to allow a choice if it would increase racial imbalance), nor can it be refused by the district or school to which the child is going, so long as space is available. However, in this same state, some districts do not allow choice among schools within the district. This can produce a curious anomaly, in which a student in a district with three schools, for example, near another district with three schools, can attend either the school to which he is assigned or any of the three schools in the next district, but cannot attend either of the other two schools within his district.

In addition, there are other variations. Of the two largest cities in Minnesota, one (Minneapolis) allows transfer from the district only if the transfer does not increase racial imbalance, while the other (St. Paul) allows unrestricted transfers. Thus even within this state with a policy of "public school choice," the extent and conditions of parental choice of school cover a wide range.

What I want to do here is to give some sense of how best to address this issue. It is an issue, in the end, of just where certain rights should lie - the rights to determine what school a child will attend. But beyond these specific rights, which take as given a particular set of schools and particular laws about compulsory school attendance, are broader rights, the rights to shape the schools and rights to determine just what kind and amount of education a child should have. These rights have for some time been in contention. The prospect is that they will become even more in contention, as the family's hold on its children in modern society weakens, and as the family itself becomes weaker and less stable.

Thus we have some interesting questions, questions that become more pressing with each decade, questions that have both sociological and philosophical components, but questions that may draw deeply on our reserves of knowledge in both these areas.

These are not merely "interesting questions." They concern the future shape of the microstructure of American society. The family's role in that microstructure

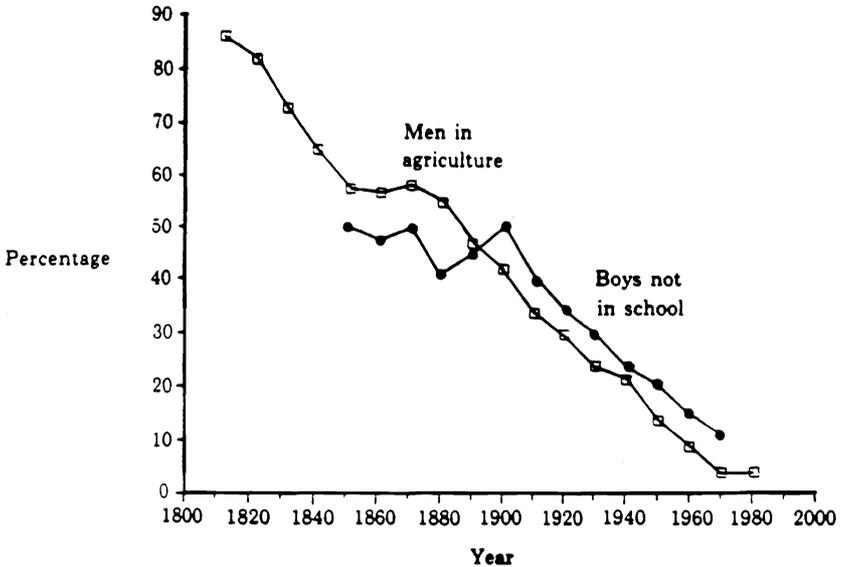
is increasingly problematic, and as a result, the question of how children will be brought up is increasingly problematic. These questions of public policy can be put in a simple way: What distribution of property rights over children will optimize the quality of the next generation? Putting the matter this way does of course sweep under the rug many questions, such as the question of how quality" of the next generation is defined. However, those questions can, I believe, be kept under the rug at this early stage of addressing the overall question.

I will begin by reviewing a part of the history of the question of rights over children's education in the United States. I will refer to those rights as they exist in Europe and elsewhere, but only obliquely, as the contrast they provide gives some aid in understanding the issues.

The first point that I wish to make with respect to the history of these rights is that the conflict over "the rights to shape children," as I will put it, is of relatively recent origin. Until the 19th century, most households were subsistence households, which meant in effect that they were semi-independent economies, each responsible for its own children, and each with authority over its own children. The family's rights with respect to its children were not challenged until the 19th century, when the economies of different households began - as a consequence of the Industrial Revolution - to be more dependent on one another. A good indicator of this growing interdependence is the decline in the proportion of households engaged in agriculture. *Figure 1* gives a sense of this decline, and of the movement of children's training beyond the authority of the household. It shows the proportion of the male labor force in the U.S. engaged in agriculture from 1810 until the present, and the proportion of boys age 5-19 in school from 1840 until the present. What is striking is the degree to which the proportion of boys not in school conforms to the proportion of men in agriculture. As men move from farming to industry, boys move from the household to schools.

In different countries, this move has a different character. In both Europe and North America, the churches were first to absorb the responsibility for education of the children; but the state was not far behind. In the United States, the movement of the state into this arena took the form of a movement to the "common school." This was a struggle against, not the family but the family's extension, the church, which for the state posed the threat of divisiveness. For a country of immigrants, each group bringing with it its own religious denomination, the threat of church schools was a strong threat indeed. It led not only to the ideology of the common school (which was most often stated in social class terms - the banker's daughter and the baker's son should be in the same school - but was more fully a reaction against religious education); it led also to a melting pot ideology, in which the "common school" was seen as a crucible in which national, family, religious, and economic differences would be melded into a single American identity. It led, beyond this, to an interpretation of the constitutional separation of church and state as a prohibition of public support of church-related schools. In some European countries faced with religious division

Figure 1
PERCENTAGE OF MALE LABOR FORCE WORKING IN AGRICULTURE,
1810-1980, AND PERCENTAGE OF BOYS AGED 5-19
NOT ATTENDING SCHOOL, 1850-1970.



Source: U.S. Bureau of the Census, *Historical Statistics of the United States, Colonial Times to 1970*, 139, (Tables D167-181 and D182-232), Washington D.C.: Government Printing Office, 1975. U.S. Bureau of the Census, *Statistical Abstracts of the United States*, 417, (Table 693), Washington D.C.: Government Printing Office, 1984. For the data on boys' school attendance, U.S. Bureau of the Census, *Historical Statistics* at 370 (Table H433-441).

in education, the solution was different. In the Netherlands, for example, the conflict between Catholicism and Calvinism for control of education led to public support of state schools, to religious schools of both denominations, and more generally, to any school that a group of parents would propose. Most recently, with Indonesian immigrants, this has led to Muslim schools.

But the separation of church and state in American schools was only one component of the state's arrogation to itself the right to determine children's schooling. In the last quarter of the 19th century, a time at which the graph showed that schooling was becoming a prominent locus for children, the South was accommodating to the elimination of slavery. One such accommodation was the passage of state laws requiring racial segregation of schools. Although these laws were responsive to popular pressure among white families, they constituted another imposition by the state of authority over where and how children will be educated. This can be seen by the lawsuit in education that was decided in 1954 by the U.S. Supreme Court: Parents of a black child who was being bussed past an all-white school to a more distant all-black school in Topeka, Kansas, sued to acquire the right to send their child to the school attended by whites, that is, to acquire the right to attend school regardless of race. In Topeka, as elsewhere in the South, children were assigned to school according to place of residence through dual districts: one set of attendance zones for assignment to the all-white schools, and one set for assignment to the all-black schools.

The Supreme Court decision did give this right to parents, by striking down the state's right to use race as a criterion in school assignment. This decision was complied with almost immediately in border states like Maryland, Kentucky, Missouri and Kansas. However, the Court had softened its ruling by not requiring immediate desegregation, and states of the Deep South did very little for more than ten years, till the late 1960s. During that period, there were attempts to satisfy the law by "freedom of choice" plans, in which children would no longer be required to attend a particular school, but could choose to attend a school other than the one attended under the segregated dual districts.

Freedom of choice in effect took the right of assignment out of the school district's hands, giving that right to parents. It is instructive to see what happened, and why freedom of choice plans were disallowed by the courts. In most districts, these plans did not bring about rapid desegregation, for one or more of the following four reasons:

1. In some districts where the child was initially assigned to the previously segregated schools, the right was not made fully available. A parent's request for transfer from the previously segregated school was sometimes discouraged or even administratively sidetracked.

2. A move to a school previously attended by the other race had to be initiated by parents. But parents were sometimes reluctant to do this because of a possible negative reception at the new school, or for other reasons.

3. Even if all parents chose the school nearest to their residence, some

segregation would remain, because of residential segregation. This was especially true in cities.

4. Freedom of choice not only gave black parents the right to send their child to a school of choice. It did so for white parents as well. Thus where white parents were opposed to racial integration of schools, they were able to flee from a school that appeared to be becoming predominantly black.

The last of these causes of the failure of freedom of choice plans to bring about effective desegregation of the schools is especially instructive. By taking the right to assign children to schools from the state and giving that right to parents, the legislature may be giving to black parents no greater right than they had before, depending on the actions of white parents. White parents, with generally higher incomes and greater social capital in the community than black parents, are better able to implement their wishes. This means that if they wish to flee from a school with black children, thus maintaining segregation, they are better able to implement their wishes than are black parents who wish to have their children in an integrated school.

As this case illustrates, reallocation of rights does not always bring about an effect favoring those to whom rights are reallocated. First, rights are often ineffective unless accompanied by resources -- in this case the financial resources and the alertness to exercise choice; and second, a reallocation of interdependent rights (as the rights in this case are) may be to parties who have conflicting interests.

It was only freedom of choice plans that failed to meet the court's approval: it became clear in the mid-1960s that in middle-sized and large cities, school districts which eliminated segregation through replacing the dual attendance zones by unitary attendance zones and thus becoming "unitary districts" did not bring about extensive desegregation. Residential segregation was sufficiently pronounced that a considerable amount of racial imbalance in the schools remained. Then, in 1969, courts took an additional step, in exactly the opposite direction from the freedom of choice plans. They *reduced* parents' rights concerning choice of their child's school. Beginning in Charlotte, North Carolina in 1969 and extending to other cities not only in the South, but in the North as well, courts ordered citywide bussing of children to achieve a racial composition in each school which approximated that of the school district as a whole. With this move, assignment of children to schools had come full circle. In 1954 in Topeka, Kansas, and elsewhere throughout the South, black and white children were being bussed past schools nearest their homes in order to achieve segregated all-black and all-white schools. By 1970 in Charlotte, North Carolina, and elsewhere in the United States, black and white children were being bussed past schools nearest their homes for exactly the opposite reason: in order to achieve racially integrated schools having similar racial compositions. Both of these assignment patterns restricted parents' choice more than had been characteristic of American education. The first pattern did so in pursuit of a

social goal of racial segregation, and the second did so in part in pursuit of another social goal, this time a goal of racial integration. In the meantime, there had been brief experiments with *greater* parental choice than had been characteristic of American education. This twisting and turning, this flip-flopping of public policy to achieve social goals, raises again the question beyond the issue of racial segregation and integration, a question about the appropriate allocation of rights concerning children's schooling: What rights should parents have, and what rights should the state have?

This question can be seen through a different prism with the issue of home schooling. Home schooling is the practice of schooling children at home, at the hand of the parents. This is not a practice that is popular among urban dwellers who go out to work each day, and would find it extremely inconvenient if their children did not as well. (Parenthetically, I might note that a good indicator of this is the clamor that arises from parents when there is a teachers' strike in a city school district: Most parents cannot tolerate their children being home rather than in school.) There are, however, parents who prefer to continue the preindustrial pattern. Their reasons are various: For some, it is religious convictions that they wish to transmit to their children. For others, it is a distrust of the capability of the public school to educate their children well. Yet some states have laws that disallow home schooling altogether, while others require higher certification of parents as teachers than is required in some of the public schools in that state.

Why does the state presume to hold the right to oversee the child's educational experience? There may be several answers to this question, but one allows us to see the difference between the child's interests and those of the parent. In some states where home schooling is restricted, the history of the parent-state conflict is clear: The parent needs the child to aid the household's economy, and uses the child to aid the household's economy without regard for the child's welfare. The parent exploits the child, and the state acts as the child's agent, to protect the child's interest in the face of this exploitation. But should the state have the right to intervene as agent of the child? And what is the criterion for answering this question? If the criterion is the child's welfare, then what is necessary is to measure the performance of the state - not the ideals behind state intervention -- against the performance of the family -- not the ideal family. At issue is a fundamental question: Whose claim to rights over the child's development should hold? Further insight into this question can be obtained by examining what has transpired in school desegregation policy and practice since the massive bussing policies of the early and mid-1970s.

In the large cities of the United States, there was a strong reaction to the strong policy of citywide bussing. The reaction was on the part of whites, and it was an exercise of choice. Here, however, the choice was exercised through choice of residence. The policies which brought citywide bussing did not eliminate parents' possibilities of choice of their child's educational experience, except for

those parents without resources.

For example, in Boston, Judge Garrity imposed a policy of citywide bussing to achieve racial balance, through a two-stage process, the first stage in 1974 and the second in 1975. Over those two years, the Boston school system lost one third of its white students, as their parents exercised choice through leaving the school system, primarily for the suburbs. A similar pattern occurred in other cities, resulting in an exacerbation of the pattern of residence which segregated black families in the central city, ringed by suburbs populated by white families.

Again with this episode, the question arises: Should the state have the right to assign children to schools against the will of the parent? If the criterion is the result, that is, the performance of the state, then the answer can hardly be an unqualified yes.

The policies of citywide bussing, although they still continue in some cities, have seldom achieved their goal of bringing stable racial integration of the schools, and have exacerbated residential segregation of metropolitan areas. Curiously, and ironically, there has been one form of desegregation policy that has shown relative success in increasing school integration in cities. This is a policy of so-called "magnet schools," having different, and somewhat specialized programs, which children can attend independent of their place of residence in the city. The policy is reminiscent of the earlier freedom of choice policies that were rejected by Southern courts in the 1960s, with the added element of specialized curricula to give the schools an attractiveness based on curriculum designed to overcome attractiveness based on the racial composition of the student body.

This brings matters nearly to the present. In the early 1980s, when dissatisfaction with the public schools was especially high, research showed that private sector schools, including both religious and secular schools, produced higher achievement, with lower proportions of students dropping out of school before graduation, for students from comparable backgrounds and abilities, than did public schools. This research fuelled a movement, already in existence, to remove the financial barrier for parents choosing a school other than a public school. The barrier consists of the full costs of schooling, since private sector schools receive no state funds in the United States. One response of public school administrators and legislators has been to increase the attractiveness of the public sector by introducing widespread opportunities for choice within the public sector. This is most often intradistrict choice, extending the idea of magnet schools throughout school district, which usually coincides with the city.

In some states, however, choice across district lines is becoming possible, following the pattern I described for Minnesota earlier. Altogether, the movement for parental choice of schools, including choice within the public sector, choice of private schools run by religious bodies, and choice of secular private schools, all

supported by public funds, is a strong movement. Predictably, the interest in home schooling is confined to a very small set of parents; but that movement has gained strength as well. Despite this strength, choice of schools without tuition payment is currently confined to the public sector throughout the United States.

Where should rights to determine a child's schooling lie?

This brings us back to a normative question: With whom should the right to determine a child's schooling lie? With the parent, with the state, or elsewhere? This question appears answerable only in value terms, but there may be means by which one can arrive at an answer, a means that does not depend on values. One approach derives, quite indirectly, from the economist, Ronald Coase, who recently received the Nobel prize in economics. The general principle enunciated by Coase (and sometimes called "the Coase theorem") is that rights should be in the hands of those who value them most highly -- and further, that if the rights are not in those hands, they will come to be in those hands through exchange, assuming the absence of transaction costs. Coase never applied his theorem to the question of property rights over children, but clearly if he had done so it would have become apparent that the transaction costs to gain those rights are in this case quite high. The rights do not always gravitate, through exchange, to the hands of those who value them most. They tend to stay, despite the movement of residence by some parents to exercise choice, in the hands of those to whom the institutional arrangements have allocated them.

What makes the Coase theorem applicable here is the simple fact that a person, depending on how that person has been brought up, imposes costs on others and confers benefits on them. The costs and benefits are perhaps greater for the family than for anyone else, but the total costs and benefits may be spread far and wide. This was not so when households were semi-independent subsistence households. Then one could say that only the family had a strong interest in how the child was brought up. Now one can say that many others have such an interest. Taken collectively, that interest can even be roughly measured. It lies in the social costs of the child's being brought into adulthood -- among which educational costs are the most prominent -- , in the costs that this person as child and adult will impose through crime and imprisonment, through publicly paid health costs, through welfare and unemployment compensation -- and on the other side, benefits in the form of taxes collected from the income earned, once the person becomes economically productive.

As this list indicates, the state does indeed have strong interest in how each of the persons residing within its borders is raised. That interest can be expressed in monetary terms, as hundreds of thousands of dollars or pounds or francs or deutschmarks. This interest lies in the dual fact of the state taking responsibility for each person through a health-and-welfare safety net and exercising the right to a portion of the person's income through taxation. At the

same time, the family's responsibility for its children during their childhood and adulthood has diminished. What was once the internal economy of the family, extending over generations with economic responsibility of parents for children in youth and children for parents in old age, has become an external economy, with responsibility in considerable part taken over by the state. There has been a partial reallocation of property rights, with the state claiming authority over children's education through compulsory school attendance laws. But property rights over children remain primarily with parents, for it is parents who determine whether a child will respond to schooling, through the kind of home environment they provide, and more generally, whether the child will become a productive member of society. Yet parents have lost most of the economic interests they once had in their children. Putting it in Coase's terms, children are of much less value to parents than was once the case. The economic value of rights over children to the state is much greater than their economic value to parents. This would seem to imply that economic efficiency would dictate giving full rights over children to the state. However, even apart from the visions of an Orwellian state that this suggests, there is the simple fact that the state is incapable of exercising its property rights over children effectively. For example, numerous studies have shown that a) variations in home environment are of considerably greater importance for variations in academic achievement than are variations among schools; and b) variations in per pupil expenditure, which is the one direct lever the state has, make almost no difference in achievement. But a different solution to the Coase problem can be for the state to exercise its interest in the child (an interest that can be calculated through a prediction of the net costs or benefits of the child to the state in each year of its life -- first, schooling costs, and later welfare costs and tax benefits) through re-creating an interest on the part of the parent. The state can offer a "bounty" for each child to the parents, for a portion of the benefits the child brings to the state beyond those predicted for the child, or for a portion of the unrealized costs of the child to the state below those predicted for this child. The bounty is a payment to the parents if the child is more productive (or less destructive) than predicted, an extra tax on the parents if the child does worse than predicted. If the parent accepts the bounty, the parent gains the right to choose the child's schooling and educational environment, receiving as the bounty in early years the child's educational cost to the state, from which the parents would pay for the child's education. As the child grows older, parents (or those to whom they sold these rights) would receive a portion of any savings achieved because the child cost the state less or benefitted it more than predicted. If the parent refuses the bounty, the child is educated as at present, in public schools paid by the state or in private schools paid by the parents.

I will not extend this venture into "bounties for children" any further. I have gone this far primarily to indicate the nature of the problem: that property rights with respect to children are improperly placed. Those who hold the property rights, that is, parents, no longer have an economic interest in their children's productivity, as they did before the changes that the Industrial Revolution has

brought in its wake. Yet parents still hold the capacity for determinizing outcomes for children. The property rights will once again be in the proper place if public policy acts to restore the parents' interest in the child's future.

Ethnic Conflict and the Politics of Race in the United States

David O. Sears

My purpose here is to share some thoughts about ethnic conflict in the U.S., with a particular focus on how it is playing out in politics. I need to confess at the outset that discussing this topic is like the old story about the blind men touching the elephant: it can be described in many ways depending upon one's perspective, and these comments will reflect my own, though it reflects the research done by a large number of contemporary social scientists.

Historical Background

Let me begin with a little history to focus attention on the distinctive historical experience of African-Americans in particular. It is that experience that has given rise to our oldest and most difficult ethnic conflict.

For convenience it can be divided into six historical periods. The first goes back to the beginnings of the slave trade in the 17th century, nearly four centuries ago. Whereas white indentured servants were relatively quickly assimilated into the mainstream of the society, as were other immigrant minority groups such as Catholics and Quakers, Germans, Frenchmen, Spaniards, and the Dutch, Africans were not. Indeed at the pivotal moment of nation-building, in the late 18th century, African-Americans were singled out in the Constitution for special treatment; like women and children they were given only partial rights, but unlike them, they were counted as less than one human being each.

Half a century later, a great protest movement arose, with the Abolitionists forcefully protesting the treatment of the slaves (no longer Africans now, but African-Americans). Two decades later, our civil war led to the emancipation of the slaves and to numerous revolutionary experiments that now go under the name of Reconstruction. Soon, however, the Compromise of 1876 ended all that, and restored the system of white supremacy to the South with the major exception of emancipation itself (and some constitutional amendments whose true import did not surface until nearly a century later). Despite the great continuities in treatment of slaves and their freed descendents, it is conventional to treat pre- and post-Civil War periods separately.

Little changed for the next 70 years. But the publication of Gunnar Myrdal's *The American Dilemma* in 1944 marked the beginning of a third period, a significant era of change in American race relations. During the next 25 years, the Southern system of white racial supremacy and formalized segregation was effectively overthrown. A few examples will remind us of the momentous nature of the changes that ensued. When Myrdal published his book, ironically enough in the midst of a war now conceived of as a democratic response to racism, consider the American institutions that were formally racially segregated into all-

white or all-black spheres of life: the armed forces, federal housing, all professional sports (including baseball and basketball), Southern public schools from kindergarten through Ph.D. programs, and, by and large, the right to vote and hold public office in the South. In the next twenty-five years, that entire system of enforced segregation dominant for over three centuries effectively disappeared.

In the course of that overthrow, the role of race in politics dramatically changed as well. As late as 1960, the two great American political parties were not seen by the general public as differing greatly on the issues surrounding the systematic deprivation of this racial minority. But a very brief period of intense activity, from about 1962 through 1965, marked by the late-blooming support of the Kennedy Administration for the Civil Rights Movement, the vigorous lobbying for civil rights legislation by Kennedy's successor, Lyndon B. Johnson, and the outspoken opposition to it by the 1964 Republican presidential nominee Senator Barry Goldwater, sharply polarized the two parties over the question of race for the first time in nearly a century.¹ Landmark civil rights legislation was passed in this brief window of opportunity, under the leadership of a Democratic party with unusual political dominance (dominance resulting from an assassin's bullet, and which no party has had since), legislation that has shaped race relations in America ever since.

A fifth period followed almost immediately, one of greatly rising racial tensions. The passage of that civil rights legislation in 1964 and 1965 was quickly followed, ironically enough, by large-scale ghetto rebellions on the part of blacks. No comparable uprisings have been instigated by other ethnic groups in the United States, to my knowledge. The first with widespread and extreme violence occurred in Los Angeles, the Watts riot of 1965, which lasted for nearly a week and cost 34 lives (see Sears & McConahay, 1973). But others followed, particularly those in 1967 in Newark and Detroit that led President Johnson to appoint the National Advisory Commission on Civil Disorders (the "Kerner Commission").

Racial tensions increased through that period from other sources as well. The non-violent civil disobedience movement in the South, led by Martin Luther King, Jr., gradually became replaced by an increasingly militant and nationally-based black movement. Among whites, George Wallace ran strong insurgency political campaigns, a populist mixture of racial backlash and anti-government feeling, first in protest of Lyndon Johnson's civil rights policies in the 1964 primaries, then as a presidential candidate in 1968, then again in the Democratic primaries in 1972, when he was shot and immobilized as a national leader.

I believe a sixth period, of growing conservatism on race, began with those George Wallace candidacies, and the Republican party's decision after its hair-raisingly close victory in 1968 not to be outflanked again on the nativist right. In the policy arena, affirmative action programs became increasingly controversial. Court judgments mandated increasingly unpopular busing programs to promote school desegregation, in 1971 extending into Northern districts characterized

principally by de facto segregation. Crime increased in urban areas throughout the country, and "law and order" began to appear prominently on politicians' agendas, with many suspecting that it was merely a codeword for race. The black underclass grew as America's industrial base fell, as W.J. Wilson has indicated (1987), and that has exacerbated many preexisting problems.

There can be no question that ethnocentrism and nativism have been strong streaks in the American psyche since the founding of the nation (see Higham, 1985), resulting in prejudice at one time or another against virtually every ethnic group other than English Protestants. And many have tried to turn such ethnic divisions to partisan advantage, whether against Catholics (in the mid-nineteenth century or in 1928 or in 1960), Germans (in the 1910s), Jews (especially in the 1930's) or Italians such as Geraldine Ferraro and Mario Cuomo. But throughout, I would suggest, African-Americans have had a unique role among all of the United States' many ethnic and racial groups. There has always been something distinctive, and stronger, about the majority white population's attitudes toward African-Americans. They do not merely reflect generalized ethnocentrism or authoritarianism; they are specifically anti-black. All other immigrant minorities have undergone substantial integration and assimilation with time; only blacks have remained significantly and persistently segregated. It is that phenomenon I want to address here.

Whites' Racial Attitudes: Change or Resistance?

Let me begin by sketching out briefly what has changed, and what has not changed, in whites' racial attitudes since World War II.

For one thing, there has been a profound, long-term liberalization in the acceptance of general principles of racial equality. Most white Americans supported legalized segregation and discrimination before World War II, and believed in whites' racial superiority and in the legitimacy of white racial supremacy. This can be seen on such issues as belief in innate racial differences in intelligence, support for laws forbidding racial intermarriage, unwillingness to vote for a black for president, and support for housing segregation (Bobo & Kluegel, 1991; Kluegel, 1990). There is dispute about whether this complex of attitudes is best described as "old-fashioned racism" (Sears 1988, McConahay 1986) or opposition to "general principles of equality" (Schuman et al., 1985), but there is general consensus that it has virtually disappeared.²

This is a major change and an important one. In politics, it has meant that blacks today can be elected in a quite wide variety of constituencies. Though race continues to play a significant role in elections with black candidates, it is no longer such a profound one that it limits them to majority-black districts. There are black congressmen in districts that are mostly white, mayors of cities in which blacks form a relatively small minority, a black governor in a largely white Southern state (indeed the former capitol of the Confederacy), and a near miss in

our largest state (in which blacks are a small minority).

A second point, however, is that there is continuing indication of severe racial polarization over racial issues. This appears most visibly in cases of inter-racial violence, such as in New York in the Bernhard Goetz, Tawana Brawley, Howard Beach, Central Park Jogger, or Bensonhurst cases. A good example is the Rodney King case in Los Angeles. In the aftermath of his televised beating by Los Angeles police officers in 1991, the black mayor Tom Bradley forcefully attacked the police chief for his lack of control over the police force. Blacks supported the mayor by a 65% to 11% margin, but Anglos supported the police chief by a 57% to 32% margin (Los Angeles Times, April 6, 1991).

Severe racial polarization can also be seen on more general racial issues. In 1967, the Kerner Commission described "Our nation [as] moving toward two societies, one black, one white -- separate and unequal" (1967, p.1). Today there is ample evidence about how differently blacks and whites perceive the presumably common real world they share. Whites believe that progress is being made in reducing racial inequality, that discrimination has been greatly reduced, and that equal opportunity does in fact exist. In contrast, blacks believe that discrimination remains at high levels, that opportunities are not equal, and that things are not especially getting better for blacks (Hochschild & Herk, 1989). For example, in a May 1991, national survey, 79% of whites thought blacks were better off compared to ten years ago, whereas only 48% of blacks agreed (NBC News, May 24, 1991).

Part of the problem is that incidents of prejudice and discrimination are simply subtler and more complex to analyze than they were in the palmy days of Southern Jim Crow segregationism. As a result they are more underground and harder for whites to see. Blacks experience it directly or hear about it directly from their friends; whites do not. Incidentally much the same problem may exist with respect to the two sexes and claims of sexual harassment. But the fact remains that the two races perceive the quality of race relations very differently.

Finally, there is evidence in five discernible areas of significant continuing racial antagonism among white Americans:

(1) There obviously are pockets of very real and simple racial prejudice in our society. The direct transcripts of recorded conversations between Los Angeles police officers during and immediately after the Rodney King beating in 1991 are chilling. And whereas surveys detect very little of this "traditional racial prejudice" among young white Americans, it is still discernible in those over the age of fifty (Bobo & Kluegel, 1991).

(2) Racial stereotypes remain. Bobo and Kluegel (1991) have found that whites continue, on average, to perceive blacks as poorer, lazier, more dependent on welfare, less intelligent, and more violence-prone than whites. Those stereotypes are not universal or categorical, but they are there.

(3) There is significant, often majority, resistance among whites to re-distributional government policies that would promote racial equality. Many, if not most, whites are opposed to actions that would redress racial inequalities, such as busing children for school integration, affirmative action, actively enforced fair housing legislation, or siting public housing in suburban areas. Busing for racial integration has been opposed so strongly by whites, and even violently at times, that it has essentially been abandoned as a mechanism for redressing segregation (see Sears & Allen, 1984, for a treatment of this issue). Whites generally support affirmative action policies that prevent discrimination against women and minorities, but they oppose those that would insure that certain quotas of minorities receive employment or entry into training or educational programs (Lipset & Schneider, 1978). And indeed opposition to such affirmative action policies of preference may actually be hardening (Los Angeles Times, November 5, 1991, p. A21).

(4) Black candidates do better these days, but still frequently have a rough ride in three ways. First of all, in many elections involving black candidates, the races split quite sharply, and relatively few whites vote for the black. This was most obvious in the divisive Harold Washington (mayor of Chicago) and Jesse Jackson campaigns (Kleppner, 1985; Sears, Citrin, & Kosterman, 1987). Even the close races run by David Dinkins for mayor of New York City, Douglas Wilder in Virginia, or Harvey Gantt for senator in North Carolina were all marked by *relatively* weak support among whites relative to party identification or past races by analogous whites. A possible exception is Tom Bradley's more recent races, including his nearly-successful 1982 run for the California gubernatorial office (Citrin, Green, & Sears, 1990). Second, racial attitudes are a strong predictor of whites' support for the black candidate in all these cases, indicating that race is an important factor. And third, there is the recent Louisiana campaign for the U.S. Senate by David Duke who, like such earlier white candidates as George Wallace, Sam Yorty, and Louise Day Hicks and Frank Rizzo ran on a barely disguised platform of hostility toward blacks. In his case it was less disguised than usual. I will return to this.

(5) Ethnic and racial hostilities are beginning to show up with respect to other ethnic groups and other issues. Perceptions that Asian and Hispanic immigration is having a negative effect on the country contribute to support for English as an official language, and to opposition to voting rights for non-English speakers and to bilingual education. Whites are more likely to support such monolingual policies than Asians or Hispanics (Citrin et al., 1991). Both symbolic racism and antagonism specifically against Hispanics contribute to opposition to bilingual education, especially the version of bilingual education that advocates cultural maintenance (Sears & Huddy, 1992). Opposition to Indians' historic treaty rights has much to do with prejudice against Indians (Bobo, 1991).

Note here that there is markedly less concern about Asians than about Hispanics or blacks. They are less negatively stereotyped than either (Bobo

& Kluegel, 1991), and the impact of their immigration is viewed much more favorably (Citrin et al., 1990).

Opposition to Racial Policies and Black Candidates

What can we say about the origins of whites' opposition to racial policies and black candidates? There are a number of conflicting theories, and not all who research the question are agreed.³ Nevertheless, I think some things can be said with confidence.

Is It Racism?

In our own work, we have defined racism fairly narrowly, as a categorical affective response to a particular group (see Sears & Kosterman, 1991). And we have found that racism contributes centrally to such opposition. But there are those who strongly believe that non-racial factors are mainly responsible. This view takes three main forms. One is the notion that opposition to racial policies and black candidates stems simply from their intrinsic ineffectiveness or poor quality. People can and do oppose bad policies and bad candidates because of their honest appraisals of them; perhaps busing, affirmative action, and Jesse Jackson fall into that category (Roth, 1990).

A second version focuses on racially-neutral values and attitudes, such as opposition to excessive government power (Margolis & Haque, 1981), individualism (valuing self-reliance and responsibility, how much the society should enforce equality as opposed to leaving it up to individual striving, and so on; Sniderman & Hagan, 1985), or ideological conservatism (perhaps especially among the better-educated; Sniderman et al., 1984).

And a third views such opposition as stemming from beliefs about the stratification system in our country: whether you get ahead by individual striving, or whether the disadvantaged are held back by discrimination and so on. Kluegel (1990), for example, has shown that the dominant explanation among whites for blacks' economic disadvantage is individualistic: either that blacks do not have as much ability as whites (favored by older whites), or that they simply are less motivated and so do not work as hard (favored by younger ones).

These race-neutral values, attitudes, and attributions all can be shown to correlate with opposition to racial policies, and in all likelihood are important factors in contributing to it (Sears, 1988; Sears & Kosterman, 1991). But I believe that a major additional factor is racism, pure and simple. Part of this opposition is specific to policies explicitly (or widely perceived as) targeting blacks in particular (and other minorities, to a lesser extent). This direct role of racism has, I believe, been fairly thoroughly documented now, using controls for other variables and explicit measurement of racial attitudes (Sears & Kosterman, 1991).

It is this *joint* effect of non-racial attitudes and simple racism upon opposition to racial policies and black candidates that has led us to talk about a "new racism," or what we have called *symbolic racism* (Sears, 1988; Kinder & Sears, 1981; Sears & Kinder, 1971). This concept ties together both simple racism and non-racial attitudes. Considerable research has found that symbolic racism is a major determinant of opposition to racial policies and black candidates, and a considerably stronger one, today, than old-fashioned racism or simple anti-black antagonism (Sears & Kosterman, 1991). In its original incarnation, symbolic racism was thought to implicate anti-black affect and individualism. But more recent research suggests that egalitarianism, rather than individualism, is the most potent racially-neutral value in it (Sears & Kosterman, 1991).

But what are the limits of the direct effects of racism? That is less clear. The broadest claim is that made in an article by the journalist Tom Edsall (1991), whose title quote is, "When the official subject is presidential politics, taxes, welfare, crime, rights, or values . . . the real subject is race." Can that be verified empirically? Racism certainly does play a major role in issues such as busing or affirmative action or opposition to Jesse Jackson, all attitude objects with manifest racial content. Racism is also central to attitudes toward law and order and welfare, which, while they often have no manifest racial content, have a widely understood racial substrate or what we have described as a "consensual latent schema" (Sears & Huddy, 1990; for the data, see Sears, Lau, Tyler, & Allen, 1980; Sears & Citrin, 1985; Smith, 1987; Sears & Kosterman, 1991). And we have found that the effects of racism extend even into campaigns that have little or no manifest racial content, or even any very obvious latent racial content, such as campaigns to cut government spending and taxation (Sears & Citrin, 1985).

On the other hand, anti-black affect or old-fashioned racism, considered all by themselves, do not directly affect the full set of partisan attitudes that Edsall described. There seems to be no major *direct* effect of racism on such core political attitudes as ideology or party identification, or on ostensibly racially-neutral values such as individualism (Sears & Kosterman, 1991). Nor did the candidacy of major white conservatives such as Ronald Reagan appear to be affected much by whites' racial attitudes (unlike that of Jesse Jackson, and to some extent, Walter Mondale; see Sears et al., 1987). So there are limits to the direct effects of racism. But when race is considered *in conjunction with* non-racial conservatism, it gets to the very heart of American politics, as Edsall says. A black man named Willie Horton by himself is not politically evocative; a black man who has raped a white woman and then been released from jail via a permissive liberal penal policy is. A TV commercial about a white man who loses his job does not evoke racial attitudes, but one about a white man who loses it because of a racial quota system does.⁴ And race is central in both cases; neither event has great political punch without the racial element.

Parenthetically I might note that there is a growing consensus that the core political attitudes in American society are indeed strongly influenced by a joint

function of something racial and something non-racial. There is more dispute about the nature of the non-racial element and what to call the result, whether it is to be called "symbolic racism," or "aversive racism" (a combination of negative racial affect that distances whites from blacks, and a commitment to the principle of equality that argues for equal treatment; see Dovidio & Gaertner, 1986); "ambivalent racism" (a combination of sympathy for blacks' plight with the belief that they have contributed significantly to it; see Katz et al., 1986); or "stratification ideology" (attributions of blacks' disadvantage to internal factors such as lack of motivation; see Kluegel, 1990; Bobo, 1991). But all these have in common the goal of offering a portrait of a "new racism," one that combines old-fashioned racial prejudice with non-racial attitudes.

And, finally, a desire for white racial solidarity is *not* a major factor at the heart of whites' racial attitudes, as far as we can tell. Numerous theories argue that it should be, such as Tajfel's (1985) social identity theory, realistic group conflict theory (Bobo, 1983; LeVine & Campbell, 1972), and fraternal deprivation theory (Runciman, 1966; Vanneman and Pettigrew, 1972). However, in our research, we have consistently found that although affect toward blacks *does* influence whites' attitudes toward racial policies and black candidates, affect toward whites *does not*, nor does affect toward whites influence attitudes toward white candidates such as Ronald Reagan or Walter Mondale (Sears & Kosterman, 1991).

Again, a qualification. We have not examined attitudes toward candidates that aggressively and explicitly advocate white supremacy and/or white solidarity, such as the early George Wallace and the latter-day David Duke, who, after all, is the founder of the National Association for the Advancement of White People. The Duke presidential candidacy in 1992 seems to have flopped, but we probably have not heard the last of the lode of white resentment that he, and to some extent Pat Buchanan, have tapped into. This may introduce a new element, therefore.

The Origins of the New Racism

Where does this new racism come from? I think we know a good bit about both where it *does* come from and where it *does not* come from. Much of it does stem from socialization in early life. We know that attitudes toward salient social groups are among the earliest products of a child's learning his or her culture. But there is now a good bit of evidence that realistic direct threats posed by blacks to whites do *not* play a major part in generating opposition to racial policies (see Sears & Funk, 1990; 1991, for reviews). Here I believe available research departs from much conventional wisdom that ties whites' political antagonism toward racially-linked liberal policies to the *personal* impact of fear of black crime, loss of jobs, "reverse discrimination" in college admissions, busing of one's own children, and so on. Indeed relatively few whites perceive racial policies as affecting their own lives very much.⁵

For example, opposition to busing for school integration jumped rather sharply in the North after the 1971 Denver case that for the first time mandated such busing outside the South (Schuman, Steeh, & Bobo, 1985). It is tempting to explain that increased opposition as resulting from the realistic threat introduced to Northern whites' personal lives for the first time. But personal threat does not explain this increased opposition to busing. The personal impact of busing did not have a significant effect on opposition to it before or after that case; nor was it linked more closely to opposition to busing after than before that date; nor did this association increase in the North after that time. Rather, busing seems to have become a highly symbolic issue in the North at that time, and was certainly used as such by conservative politicians (Sears & Allen, 1984).

Again, a qualification. I would suspect that such personal motives do play a role in some places at some times on some issues. Indeed in our own work we did find a substantial impact of self-interest on whites' opposition to busing just as the Los Angeles busing plan unfolded in 1976 (Sears & Allen, 1984). Indeed the resulting "white flight" has had a devastating effect upon a once-excellent system of public education in the Los Angeles area. And I would not be at all surprised to see the personal impact of racial issues play a larger role in the future. Admissions standards at many universities vary a good bit across ethnic and racial groups, and there is rising resentment about impaired opportunities for non-minorities. Allen Bakke initiated his landmark suit to improve his own personal situation, and as universities become more successful in diversifying their student bodies and faculties, we may see more such white backlash that is based on self-interest; i.e., on whites' experience of seeing students and faculty less qualified than they receive admission and get jobs that they want.

But, to repeat, the personal impact of racial issues is not at the moment the main force driving whites' resistance to policies enhancing racial equality. The more general theory that intergroup hostilities stem from realistic group conflict needs to be revised to take account of this general lack of any effect of personal threat. Threat to the group may be an important factor, as Bobo (1983, 1988) contends, but it is not always easy to pin down empirically. I would simply suggest that if realistic intergroup competition is a key factor, it may well be mediated more by long-held, early socialized prejudices against the group in question than by solidary feelings within the majority or feelings of being personally threatened by the minority.

Hidden Racism

It is quite clear that prevailing social norms about racism have changed dramatically. Racism is no longer widely viewed as a legitimate social idea. One important consequence is that it is no longer socially acceptable to express old-fashioned racism overtly in most social contexts.⁶ Whatever the size of the hard core of racists remaining in the society, the general norms for overt social ex-

pression have clearly changed.

Everyone would agree, I am sure, that the society is better off for having declared overtly racist statements as socially inappropriate. But has old-fashioned racism really declined, or has it simply been driven underground? John McConahay (1986) has argued that old-fashioned racism remains fairly common, but it tends not to be expressed in public because it is consciously suppressed by people who fear social disapproval. In contrast, modern forms of racism get more freely expressed because they are less obviously racist. His evidence is indeed persuasive that assertions of old-fashioned racism are widely perceived as reflecting racism, and therefore are rejected, whereas assertions of modern or symbolic racism are not (McConahay et al., 1981). So we see an increasing use of "codewords" to express racist views. David Duke speaks of a "massive rising welfare class", but this follows a long tradition enunciated by George Wallace and adopted by the Republican party, to use ostensibly non-racial issues such as welfare and law or order as codewords for race.

I think we do *not* know at this juncture how widespread this underground racism is. We do not know how much crude, old-fashioned racism is really there but slips past our survey nets, or indeed is not openly expressed in public at all. For example, I suspect that the longstanding and important declines in expressed beliefs in racial differences in intelligence may not fully reflect the persistence of such racist beliefs.

The phenomenon of systematic slippage in votes for black candidates between pre-election polls and actual election outcomes (and even exit polls) is perhaps a tangible indicator of the problem of underground racism. This held true in a number of polls in Los Angeles during Tom Bradley's early mayoralty runs, as well as for Douglas Wilder in Virginia, David Dinkins in New York City, and Harvey Gantt in North Carolina (though it could be argued that Jesse Helms' last-minute media blitz actually changed votes), and for Louise Day Hicks in Boston in the 1960's and David Duke in his 1990 race for the US Senate. Interestingly, Warren Mitofsky reports (New York Times, November 17, 1991) that exit polls were exceedingly accurate regarding Duke's 1991 Louisiana gubernatorial race, and indeed in that race, pre-election polls did not underestimate the Duke vote. But this was a case of extremely high salience and high turnout, for whatever that portends.

There are potentially serious effects of driving racism underground, however. The devil we know is easier to deal with than the devil we don't know. The occasional surges of votes for a Wallace, a Duke, or a Buchanan suggests the presence of pools of resentment and hatred in places that are wholly outside the public dialogue and the formal arenas we have for dispute resolution. Even more ominously, what happens if the effect of hidden racism is to drive people away from the use of elections as mechanisms for settling conflicts of interest? I suspect one could find evidence that it does indeed contribute to the widespread alienation from the political process that is associated with low turnout.

And we can dispute the appropriateness of enforcement mechanisms, as in the current debate about rules of etiquette on campus and charges of monitoring for the "politically correct." The bans on "fighting words" instituted at Wisconsin and UC Berkeley and other universities may be of doubtful constitutionality in any case. There certainly is a tradeoff between civil liberties and protecting women and/or minorities from embarrassing verbal expressions. The First Amendment was, after all, generated to protect disagreeable and even offensive expressions of belief.

Finally, the dangers of driving racism underground are by no means limited to our underestimating racist views among whites. As blacks have long pointed out to us, a lack of honesty about racism confuses interracial dialogue, however much suppressing its expression contributes to the momentary pleasantness of interpersonal relations. It can lead to some nasty surprises for blacks because it makes it difficult for them to know when racism really is in play. And in return it makes it too easy to attack positions disagreeable for other reasons on the basis that they are "racist." The mayor of Washington, D.C., Marion Barry, attacked prosecution of him for drug charges as based on racism. Black leaders attacked challenges of Tawana Brawley's charges on the same grounds. Those who were appalled by the Rodney King beating by Los Angeles police denounced it as racist. Charles Thomas interpreted challenges to his nomination as a Supreme Court justice as a "high tech lynch mob." Willie Brown, Speaker of the California Assembly and a black man, has interpreted attacks on his integrity and life style as based on racism. All are probably true, to some measure, but it is difficult to know how much, and sometimes hurling the charge of "racism" distracts attention from other important issues.

As a general matter, the "discounting principle" central to attribution theory (Kelley, 1972) would suggest that when two or more plausible attributions for an action exist, on the average people will divide attributions between them. So if indeed opposition to black politicians and racial policies is motivated by both racial antagonism and non-racial values, as the symbolic racism view suggests, then it is realistic to attribute it to some element of racism as well as to acknowledge the legitimate non-racial considerations. But in practice some observers interpret any given action as racitly motivated while others do not, with the difference in interpretation deriving less from reality than from political predisposition. Thomas supporters were much more likely than Hill supporters to think opposition to him was racially motivated, whatever the truth of the matter.

Is All Politics Now Racial?

The view of Edsall and others is that "all political issues have become racial," whether crime, welfare, drugs, schools, public health, unemployment, or poverty. And ideology and party identification are also said to be inextricably linked with

race. Is that true?

We know that the two political parties were not widely perceived as racially polarized prior to the Kennedy administration. At that time, the Democrats were torn internally between an aggressive civil rights faction (dating from the late 1940s) and the need to pacify the racially conservative Southern wing of the party. Until 1958, the Republicans tended to be split as well between a relatively liberal Northeastern faction and the more conservative midwesterners. But in the early 1960s, the adoption of the civil rights agenda by the Kennedy and Johnson administrations, and then, in 1964, the polarization of the two parties' presidential campaigns over civil rights legislation, led to a sharp polarization of party elites over race (Converse et al., 1965). By 1972, racial issues had an increasingly central place in the public's perceptions of differences between the two parties, with the Republicans regularly seen as more conservative (Carmines & Stimson, 1989). The candidacies of Jesse Jackson increased this perception (Sears et al., 1987).

Today the George Bush position on racial issues walks a tightrope. He regularly "plays the racial card," appealing to latent racism by opposing "quotas" and supporting law and order (especially making an issue of black sexual crime, as indicated by the Willie Horton incident and "revolving door" ads). At the same time he tries to steer clear of positions that could be denounced as sympathetic to old-fashioned racism, so he does not oppose all forms of affirmative action, or support David Duke, or fail to keep at least one black on the Supreme Court.

This partisan polarization over race was not necessarily a losing proposition for the Democrats in the early 1960's. Old-fashioned racism quickly became discredited, even in the South, as the Civil Rights Movement won the day. Being against segregation became a bit like being against sin. But the same cannot be said for the racial policies and attitudes that have been at the heart of American political controversies in the past two decades. Welfare, busing, affirmative action, quotas, reverse discrimination, and black crime all are quite unpopular. Democrats have been saddled with the losing side of all these issues.

Are the Democrats born losers? Edsall is not alone in forecasting the death of the national Democratic party as a consequence. They have been consistently weak at the presidential level since these newer racial issues attained prominence. True, the Democrats have continued to dominate at the local, congressional, and senatorial level. Maybe they simply are more adept at handling matters of day-to-day interest, as some argue. Or maybe that is just a function of historical lag, given the power of incumbency. That remains to be seen (and much will be clearer after the redistricting of congressional seats kicks in, and after the term limits in various states take effect, especially with the diminished respect given to incumbents perse).

But that "all political issues have become racial" is consistent with our data only by invoking the concept of symbolic racism. Basic partisan dispositions

such as ideology and party identification are not closely related to old-fashioned racism, but they are related to the new, symbolic racism. Similarly, symbolic racism (or a mixture of racial intolerance and race-neutral conservatism) influences preferences on such ostensibly non-racial policy issues as welfare, tax limitations, domestic spending cuts, law and order. It is the *mixture* of anti-black affect with non-racial values represented in symbolic racism that is explosive, generates polarization over the domestic issues just cited, and therefore has become central to partisan debate in our time.

Liberals frequently, and I think rightly, decry the tendency of such conservatives as George Bush, Jesse Helms, and David Duke to "play the race card" -- to interject racial themes into campaigns to get white support. But is "the race card" purely arbitrary? Could they argue the same issues without any reference to race, or could they argue other issues altogether?

There are many issues upon which the public could conceivably focus at any given time. Only some of them do indeed receive widespread public attention. And only some become salient in election campaigns. The experimental work of Iyengar and Kinder (1987) has been quite influential in documenting the power of television agenda-setting in determining which dimension gets used as a yardstick in evaluating candidates.

The experimental method randomly assigns treatments to individuals. The real-life analogue would be that reality can successfully be arbitrarily presented in many different ways. That may be a somewhat misleading model. Contemporary racism centers on things that are quite real: violent crime in the ghetto, high rates of unemployment and welfare dependency, the ubiquity of the black mother as single head of household, gang fights, drug usage, the high percentage of young black males in prison and the low percentage in college, and the like. A Willie Horton ad or Jesse Helms' anti-affirmative action ad are not arbitrarily or randomly selected; they reflect a harsh reality of modern life, and one that is well ingrained in the popular mind. There is something to the agenda-setting argument, then, but the "race card" is more than purely arbitrary; there is a reality out there, though in this case one that is socially constructed out of the normal operation of social institutions, not merely from simple descriptions of daily life.

Moreover, one of the most notable happenings of the past 25 years has been the tendency for other disadvantaged groups to model their pleas or demands for better treatment on those of the black movement. In essence the Civil Rights Movement of the 1950's and early 1960's, and to some extent black militancy of the late 1960's, have served as the models for feminists, gays and lesbians, the disabled, the homeless, Chicanos, and Asian-Americans. No longer do we have the Kerner Commission's black and white world, but one with many voices.

What can usefully be said about this wide diversity of claimants? It is not a unified protest, contrary to the dreams of those advocating a "rainbow coalition,"

beyond some temporary alliances in local circumstances. But it has had broader effects. I believe it has diffused public energy from the very real longterm problems of the black population, which are more serious than any of the others. And to some extent it has discredited remedial efforts for blacks; e.g., many more minority children must be considered in school integration, and many more women and minorities claim entitlement to affirmative action, which then makes any such social policies much more costly.

I also believe that the claims by other disadvantaged groups to the same level of redress as blacks has helped discredit the Democratic party as the party of "special interests," some of them (like gays and lesbians) quite socially unpopular. The original claims of the black population were salable, due to the uniquely disadvantaging impact of the slavery and Jim Crow experiences. It is much more difficult to sell the same message on behalf of the many immigrant groups who, while needy and disadvantaged as have been most immigrant groups who have come to the United States, face no obvious barriers greater than those of previous immigrant groups who now regard themselves as having largely assimilated (by their own efforts) into the larger society. This seems to me true even if one does not raise the issue of such claimants to affirmative action as women, the disabled, or gays and lesbians.

It also has attracted opposition from an ethnocultural conception of "American identity" (based on speaking English, trying to get ahead, voting in elections, defending America when it is criticized, and believing in God; Citrin, Reingold, & Green, 1990). A sense of American identity proves to be a significant predictor of beliefs that Asian and Hispanic immigrants are having a negative effect on our country, opposition to multilingualism (such as bilingual education, support for English as an official language, or limiting voting rights for non-English-speakers), and opposition to affirmative action for Asian- and Hispanic-Americans (also see Citrin, Green, Reingold, & Walters, 1991). To the many other burdens of the Democratic party, then, have been added that of defending what are widely regarded as unfair special privileges accorded to these other demographic groups.

For the Future

Where do we stand for the future, then? Let me make four points by way of summary.

Progress

There has been very real progress in race relations in America since 1941, incorporating blacks much more thoroughly as equals into American society. The doctrine of racial superiority is no longer regarded as a legitimate position. There has been much successful integration of the workplace, higher education, and political life.

Over the longer term, continuing changes in the nature and degree of white racism should depend in part on the socialization of young people. That in turn should depend in part on which attitude objects are salient in early life, and on the dominant attitudinal environment concerning those objects in that era (e.g., Sears, 1983). For example, the most salient racial attitude objects for whites growing up in the late 1950's and early 1960's were efforts to end the obviously unfair system of segregation in the South. The socialization environment would seem to have been less favorable in the years since then, as the salient issues turned to mandatory busing, ghetto-based crime, the media's increasing framing of affirmative action in terms of reverse discrimination against whites (Gamson & Modigliani, 1987), and the opposition of Republican administrations to various civil rights measures, on which the social consensus was less favorable to blacks.

Available cohort analyses do find that cohort replacement has operated in this period as a liberalizing force (Firebaugh & Davis, 1988; Schuman et al., 1985). Within cohorts, similarly, these studies reveal the decline in old-fashioned racism among the post-Civil Rights era cohorts expected from such a view of racial socialization. However, the results on items dealing with contemporary policy issues are more mixed: Davis (1991) has found evidence of slowing cohort differences in the post-1946 birth cohorts, as might be expected if the dominant attitudinal environment had turned less favorable to blacks (also see Steeh & Schuman, 1991).

Problems

Serious problems remain. Some are economic, but all are compounded by race. There is a nearly intractable underclass problem that is devastatingly costly to American society, breeding crime, drug abuse, generations of children who grow up in poverty, impoverishment of American cities, and other social problems too numerous to count.

And there is the David Duke phenomenon. It has in it some old and some new elements. The old element is that his support base shares much with that of other populist racial agitators of the past 25 years, such as George Wallace, Sam Yorty, and Frank Rizzo. It is clear that there is a strong racial component to white support for all of these (Kinder & Sears, 1981; Howell, 1991; Lipset & Raab, 1978; *New York Times*, November 17, 1991). Their support builds on white working class resentments of white elites, minorities, and government itself. They also appeal in particular to less educated males, and perhaps to the economically frustrated.⁷ The fact that Duke took a majority of the white vote in his recent gubernatorial race in Louisiana is not surprising in light of these other candidates, who showed the same strength in Southern and border states. The Pat Buchanan presidential candidacy in 1992 also showed many of these same elements.

What is new is the fact that Duke is more explicitly anti-black and anti-Se-

mitic than has been the case with the earlier populists who appealed to racism. This is both good news and bad news. The good news is that it makes it easier to discredit him, because of the norms of tolerance toward blacks and Jews which are now quite powerful and widespread in American society. The bad news is that he accumulates a great deal of white support nonetheless.

National Disarray

The nation seems unwilling or incapable of taking the steps that are required to deal with our racial problems. I believe much of that unwillingness has as its core antagonism toward (or at least lack of sympathy for) poor blacks, which is a long-standing feature of American politics. But it also occurs at a time of some national disarray. The economy is not doing well, and there are anxieties about American ability to compete internationally. The debt structure, private and public, makes it difficult to mount new national initiatives. There seems to be a declining sense of community, and increasing politicization of group differences. The question asked by political activists is increasingly "what is good for *my* group" not "what is good for the community or society at large." There are also signs of a nativist or racist backlash against multiculturalism. And decades of partisan political gridlock, a host of scandals, and years of political apathy in the general public have produced great losses of respect for politicians and political institutions. The political system is not well-positioned to help out very much.

The opposition party is in disarray and does not provide a credible alternative to the party in power. The public does not perceive the Democratic party as superior in handling the economy, however much confidence has been lost in Bush. The Congress, dominated by Democrats, is not viewed favorably as a collective body, for a variety of reasons.

It is the *mixture* of themes that I think must be remembered as we watch the last decade of this century unfold. Broadly-based acceptance of basic egalitarian principles is accompanied by racial antagonisms and prejudices. The political manifestations of race stem from *both* racism and core attitudes quite independent of race. But the claimants for group entitlements are proliferating, and ethnic tensions are rising. Partly this reflects more honesty about group differences, but it also reflects a declining sense of civic responsibility for the whole. It seems to me unlikely that a nativist backlash will dominate the country, but it will be heard loudly, and we will see various elements of it enacted into law.

Finally, some comments about broader social changes as viewed from our largest state, California. The rising tide of immigration into the United States, especially from Asia and Latin America, is creating some startling changes. For example, at the two largest campuses of the University of California, Berkeley and Los Angeles, the freshman class is now only one-third white; the other two-thirds are from one or another so-called minority group. In California as a whole, minorities will soon be the majority. These "minorities" are increasingly militant.

Within the Universities, "diversity" has become a buzzword, along with emphasis on race, gender, and class. But the voting population -- the electorate -- remains overwhelmingly middle class, white, and middle-aged. And such people tend to be relatively conservative and opposed to taxation. Partly this is due to general opposition to government, and part of it stems from racial antagonism (Sears & Citrin, 1985).

So the state is increasingly composed of noisy advocates of a population that requires expensive public services -- health, education, and welfare -- and an electorate reluctant to pay for them. This gap becomes increasingly visible as the total economic pie declines, with the decline in real economic growth rates. The result is a real decline in the quality of life for the citizenry, with all the civic tensions that accompany that. And there is a separation between the haves and the havenots, with Anglos and Asians increasingly in the have category and blacks and Latinos have-nots.

While racial integration proceeds, and old-fashioned prejudice recedes, then, there are counterforces that suggest continuing ethnic tensions and some inability of the body politic to deal directly with them. It is difficult not to foresee a period in which ethnicity once again becomes a pivot on which much American politics will move, a pivot riddled with social conflict.

Race-Targeting Social Policy

This would seem to be a pessimistic view for supporters of racial policies. Can it be reversed? An interesting angle is provided by the recent work of Bobo and Kluegel (1991). They attempted to construct policy alternatives that reflect the "new liberal agenda," steps to ameliorate poverty without violating individualistic values, principally by allowing people to "make it on their own" (such as enterprise zones and college scholarships). As Lipset (1991) notes, Americans generally support compensatory action, because it fulfills egalitarian values, but not preferential treatment, because it violates individualistic values. This "new liberal agenda," in Bobo and Kluegel's data, does prove to be more popular than such traditional liberal policies as providing special government aid to minorities, partly because they are less likely to attract opposition on the basis of racial attitudes.

But they find that even this "new liberal agenda" loses support when these policies are specifically targetted for minorities, as our findings would also suggest. In general, race-targeting social policy had some potential for attracting support in the 1950's and 1960's; whites could believe that blacks were disadvantaged, because of the glaring segregation they confronted. In the present climate of opinion, it is at least a subtler case, certainly a harder sell, and perhaps intrinsically a losing proposition. The failure of this sales job lies at the root of political opposition to racial policies and black candidates. It is doubly difficult because redistributinal policies also have long been a hard sell; the majority favors market, not political, remedies for inequalities (Lane, 1986). A non-race-

targeted "new liberal agenda" is a promising approach, but perhaps less because it fits with individualistic values than because it allows for natural, market-driven inequalities to emerge that can plausibly be attributed to merit.

Notes

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- 1 In truth, the seeds of this polarization had been sewn a few years earlier, as as Carmines and Stimson (1989) have shown, in the recession - stimulated Democratic surge in the 1958 congressional elections, but it was only in the 1963-64 period that the general public began to perceive significantly greater liberalism on the part of the Democratic party.
- 2 For an exception, see Sniderman & Tetlock (1986).
- 3 See, for example, Bobo (1988), Kinder (1986), Roth (1990), Sears (1988), Sears & Kostermann (1991), Sears & Kinder (1985), and Sniderman & Tetlock (1986a, b) for a flavor of these disputes.
- 4 It is less clear that the attributions described earlier as "stratification beliefs" are truly race-neutral because they do have manifest racial content. It is therefore possible that a white person who derogates blacks will do so both by decrying their ability (and/or motivation) and by opposing remedial policies. On the other hand, it is also possible that such attributions have independent causal roles in motivating opposition to racial policies, as Kluegel (1990) and Bobo (1991) believe.
- 5 Nor are negative views of Asian and Hispanic immigrants closely tied to personal economic anxieties, whether personal or societal (Citrin (ed.) et al., 1990a). Indeed whites generally do not see much immigration as actually affecting them very much.
- 6 More unacceptable for the young than the old, though; see Bobo & Kluegel, 1991; Kluegel, 1990; Schuman, Steeh, & Bobo, 1985.
- 7 The David Duke vote in Louisiana was stronger among those whose own personal finances were troubled. This is not a standard finding in the literature but it is a sign that economic tensions could fuel more racism (New York Times, November 17, 1991).

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The Impact of Foreign Ownership on U.S. Business

Rachel McCulloch

In the decades following World War II, many U.S. companies established subsidiaries abroad. The nation's role as the leading source country for outward direct investment shaped American attitudes toward foreign ownership. But during the long economic expansion of the 1980s, the tide turned. Foreign companies rushed to establish or expand subsidiaries in the United States. Foreign control of U.S. business assets increased at an unprecedented rate. By the middle of the decade, the United States had replaced Canada as the world's number one host country in terms of total value of foreign-controlled business activity.

This paper analyzes the causes of the rapid rise in foreign direct investment in the United States and its impact on U.S. business and on the nation's economic performance overall. The analysis centers on four broad questions. First, how are inward direct investments linked to other major developments in the nation's international economic position, especially the much-discussed emergence of the United States as a large international borrower and the loss of U.S. competitiveness in manufactured goods as reflected in recent trade performance? Second, what has made foreign companies so eager to invest in the United States? Third, what are the likely effects of expanded foreign ownership on the employment and wages of U.S. workers and on the return to U.S.-owned capital? Finally, how is U.S. policy toward direct investment adapting to the nation's new role as a major host country?¹

The growth of foreign ownership

As a consequence of the investment boom of the 1980s, foreign companies now play a prominent part in the daily economic lives of most Americans. When a U.S. consumer buys a new car, shops in a department store, or checks into a hotel, chances are increasingly good that the supplier will be the local subsidiary of a company based in Europe, Japan, or Canada. The same is true when a U.S. business rents office space, purchases components, or applies for a bank loan. Canadian and European multinationals such as Seagram, Shell, and Nestle are so well established on the American scene that most of their U.S. customers do not even realize they are dealing with a foreign-controlled business. On the other hand, Americans purchasing Sony television sets or Honda automobiles often assume these goods are imports - as indeed they would have been, a decade ago. Today many popular "imports" are actually produced - or at least assembled - in Japanese-controlled U.S. factories.²

Although the extent of foreign control of U.S. business began to climb during the 1970s, the issue became controversial only much later, when the

Table 1.
 FOREIGN INVESTMENT IN THE UNITED STATES:
 BALANCE OF PAYMENTS INFLOWS, 1960-90
 (billions of U.S. dollars)

Year	Total inflow	Total FDI inflow	FDI as % of total	Japa- nese FDI	% of FDI from Japan
1960	2.3	0.3	13.7	NA	NA
1970	6.4	1.5	23.0	0.0	3.6
1972	21.5	0.9	4.4	0.0	2.0
1974	34.2	4.8	13.9	0.2	4.1
1976	36.5	4.3	11.9	0.6	13.5
1978	64.0	7.9	12.3	1.0	12.5
1980	58.1	16.9	29.1	0.9	5.6
1981	83.0	25.2	30.3	3.0	11.8
1982	93.7	13.8	14.7	2.0	14.3
1983	84.9	11.9	14.1	1.7	13.8
1984	102.6	25.4	24.7	4.4	17.2
1985	130.0	19.0	14.6	3.4	17.8
1986	221.6	34.1	15.4	7.3	21.3
1987	218.5	58.1	26.6	8.8	15.1
1988	221.4	59.4	26.8	17.3	29.1
1989	216.5	70.6	32.6	17.4	24.7
1990	86.3	37.2	43.1	17.3	46.6

FDI = Foreign Direct Investment.

Source: *Survey of Current Business*, August 1991 and earlier issues.
 Percentages calculated from unrounded flow data.

Table 2.
 FOREIGN DIRECT INVESTMENT IN THE UNITED STATES:
 BALANCE OF PAYMENTS INFLOWS FOR MAJOR INVESTING
 COUNTRIES, 1985-90
 (billions of U.S. dollars)

Year	Total, all coun- tries	U.K.	Japan	Nether- lands	Canada	Ger- many	Switz- er- land
1985	19.0	4.7	3.4	2.8	0.9	2.3	2.7
1986	34.1	10.8	7.3	4.4	2.5	2.0	1.4
1987	58.1	25.3	8.8	8.5	3.7	4.4	3.0
1988	59.4	21.0	17.3	5.8	1.2	2.4	0.8
1989	70.6	18.9	17.4	7.3	3.2	3.8	4.7
1990	37.2	3.7	17.3	7.1	0.0	-0.9	-1.0

Source: *Survey of Current Business*, August 1991 and earlier issues.

trend finally caught the eye of the public, the press, and the U.S. Congress. In fact, except for transient worries about such matters as Arab purchases of U.S. land, public interest remained modest until the late 1980s. In current-dollar terms, the average annual inflow of direct investment for the years from 1985 to 1990 was more than five times as large as for the corresponding period a decade earlier. The share of Japanese-controlled investments in these larger total inflows also soared. Although many of the investments were "green-field" projects, newly constructed by foreign owners, public attention focused on foreign takeovers of existing U.S. businesses.

Until 1984, direct investments from Japan were small both in absolute terms and as a share of the total increase in foreign-controlled businesses (see Table 1). Japan's share rose to over twenty percent in 1986 despite the contemporaneous surge in inflows from other source countries. In 1990, while total inflows dropped markedly from their 1989 peaks, Japanese investment inflows remained at the same level as in 1989. This raised Japan's share in the (dramatically smaller) total 1990 inflow to nearly one-half.

Japanese investors were inevitably more conspicuous than their Canadian or European counterparts. The British, already well-established in the United States at the start of the investment boom, continued to outspend the Japanese on new investments until 1990 (see Table 2). At the end of the decade British-based firms also remained the biggest direct investors by far in terms of overall position, although the Japanese had moved into second place, overtaking the Dutch, Canadians, and Germans. However, Japanese investments aroused stirrings of public concern that Canadian and European investments did not, perhaps reflecting the link of Japanese direct investments to Japan's increasing successes in trade competition with U.S.-controlled companies.

American worries

While times were good, the United States worried mainly about the same large but somewhat vague consequences of increased foreign ownership that had worried other host nations worldwide as U.S. firms established subsidiaries abroad during the decades after World War II. Heading the list was loss of control over domestic economic activity - loss of economic sovereignty, in the usual phrase - and an associated potential threat to national security. These large issues have remained contentious in the 1990s environment of low growth and high unemployment, but the debate has refocused on the highly specific concerns of those affected most directly.

The most prominent issue is jobs - more precisely, what happens to American employment and wages when a foreign company gains control of a U.S. business. Less often raised explicitly but intimately related is what happens to profits of U.S.-controlled companies. In American politics it is fine, indeed

necessary, to worry about employment and wages, but less wise to say much about profits.³ Yet from an analytical perspective these are two aspects of a single phenomenon.

Of course, the United States is likewise worried about the nation's trade. The issues of trade and direct investment are closely linked. Like expanded imports, new direct investments represent a challenge to established domestic producers. As with competition from imports, beleaguered domestic firms are apt to label activities of their foreign-controlled U.S. rivals as unfair and detrimental to the national interest. Just as the recession of the early 1990s brought forth new calls for aggressive trade policies, critics of foreign direct investment found a host of new reasons to limit the role of foreign companies within U.S. borders. Yet the same recession also increased the zeal of those who favor an open-door policy toward new foreign investment. Indeed, with trade performance sagging and many U.S. regions and industries experiencing near-record unemployment, most states and numerous cities have dispatched missions abroad in active pursuit of new investors who would, it is hoped, create new jobs and boost industrial competitiveness. The competition to attract foreign investors has created a worry of its own. With so many states and cities bidding for new investments with special incentives, the benefits might well be shifted in favor of foreign firms and away from U.S. workers, investors, and taxpayers.

Another concern is how these investments affect America's technological edge. Does foreign ownership help to boost U.S. productivity and restore the vigor of U.S. business, or, on the contrary, do direct investments aid foreign companies in their quest for better access to U.S. technology in leading-edge products like computers and aircraft? Briefly put, Americans are now wondering whether a growing role for foreign investment is part of the solution to the nation's loss of international competitiveness, or part of the problem.

Direct investment and net capital inflows

The rapid build-up in the 1980s of foreign ownership of U.S. business occurred in the context of an explosion in two-way international trade in all types of assets. For several decades U.S. investors had dominated international financial markets as both lenders and borrowers, but with a modest net capital outflow in most years. In the 1980s the United States became a net borrower on a scale that was unprecedented for any nation. A major part of the borrowing took the form of sales abroad of U.S. treasury securities as the U.S. federal budget deficit soared. Foreign deposits in U.S. banks also soared. But these forms of net borrowing from foreign sources are quite different from increased foreign control over U.S. business activity in terms of their impact on U.S. economic performance. Although both kinds of net capital inflows were important for the United States in the 1980s, only a minor part of the rise in total capital inflows came in the form of foreign direct investment. Even in 1989, when total direct investment inflows

reached a peak of more than \$70 million, this constituted less than a third of total capital inflows for the year.

Despite the popular perception based on the 1980s that the two are closely linked, inward foreign direct investment does not typically move in lock-step with U.S. external borrowing, nor has foreign direct investment in other regions been highly correlated with overall capital flows. While the United States did experience a large increase in direct foreign investment during the 1980s, a period of large overall net capital inflows, and while the opposite held true for Japan over the same period, historically major source nations have not necessarily had overall capital outflows, and major host countries have not necessarily had overall capital inflows. During the 1970s, several OPEC nations became major foreign lenders but remained negligible as foreign direct investors.

While an investing *firm* usually needs financial capital to build or buy a new business,⁴ the firm may be able to borrow the needed funds *abroad*. U.S. companies did exactly this in the 1960s - borrowing in Europe much of the money they used to acquire a large stake in European business. Indeed, this was one of the criticisms made by Europeans at the time: Americans were controlling too much of Europe's economy, and they weren't even bringing in new capital. U.S. direct investments abroad even continued to grow at a sizeable rate during the 1980s, years of record net capital inflows.

The flood of direct investment into the United States in the 1980s is thus something that needs to be explained separately from the big rise in U.S. net borrowing. Most economists see the rise in net borrowing as the result of overall macroeconomic forces; when aggregate U.S. saving (private saving less the fiscal deficit) falls short of aggregate domestic investment, the nation necessarily borrows the difference abroad. In contrast, the rise in direct investment is basically a microeconomic phenomenon driven by competitive conditions in particular markets. To understand the causes of the direct investment surge, we must examine the motivation of individual companies.

Why foreign firms establish U.S. operations

To understand why foreign firms have been buying and building U.S. operations, it is helpful to look at direct investment as an integral part of a firm's overall strategy for global production and sales. At one level, it should not be surprising that successful firms expand their operations. When that expansion crosses a national boundary, it becomes - by definition - foreign direct investment. Yet many firms sell abroad without undertaking direct investments, and in any case investment abroad is not necessarily the most profitable avenue for increasing foreign sales. In fact, a foreign firm is almost always at some disadvantage in operating away from its home base. A foreign company's decision to invest in the United States thus raises two questions: First, why does the firm choose direct

investment over other strategies? Second, how is the foreign firm able to compete successfully with U.S. companies already established in the domestic market?

Modern theories of foreign direct investment suggest that a firm will want to establish a U.S. subsidiary only if it enjoys a firm-specific competitive advantage over its rivals *and* if that advantage is most profitably exploited through managerial control over operations in multiple countries.⁵ The same firm-specific advantage (in terms of product, process, or management) also provides the basis for multiple-location operations at home. However, direct investment in the United States can be a viable strategy only if that advantage is important enough to outweigh the firm's disadvantages relative to established U.S.-based competitors. The rapid growth of U.S. imports *and* of inward direct investment can therefore be seen as two aspects of a single phenomenon - both reflect the increased global competitiveness of corporations in Europe, Japan, and Canada in relation to their U.S.-based rivals.

Empirical studies show that direct investment activity is clustered in the industries where research and development (R&D) and advertising expenditures are important. Such expenditures presumably create a competitive advantage that allows a firm to operate profitably in a foreign environment. But a competitive advantage is still only a necessary condition for direct foreign investment. The firm's competitive advantage can in many circumstances be better exploited through exports from the home country. An additional requirement for setting up U.S. operations is a locational advantage. In the absence of a significant locational advantage, the potential investor is likely to choose exporting over the more costly and risky option of establishing a U.S. subsidiary.

A locational advantage can reflect the usual considerations of production and transport costs. Other locational advantages arise from national and local policy at home and in the United States, e.g., taxation, regulation, barriers to trade. These include both the basic policy environment and the carrots and sticks that home and host countries use for the specific purpose of influencing the location of production.

Like a competitive advantage over established rivals, a locational advantage is necessary but not sufficient. Even given a competitive advantage and a locational advantage, there must also be an organizational advantage of direct foreign investment over alternative strategies such as licensing or other long-term contractual arrangements with U.S. firms. In other words, there must be an advantage of integrated global management that is sufficient to offset its additional costs to the firm.⁶

Direct foreign investment can be viewed as the means by which a firm extends its managerial control across a national boundary. The underlying motives for such investments are therefore essentially the same ones that

promote expansion of a firm's activities within its domestic market. Because international expansion is typically more expensive, the anticipated benefit needs to be larger to offset the higher cost. This perspective is supported by the empirical finding that U.S. firms investing abroad are on average larger in their *domestic* operations than other firms in the same industry. In a given industry, multinational firms based in small countries are also typically smaller than their counterparts based in large countries. Both observations are consistent with the hypothesis that firms should exhaust most of the likely gains from domestic expansion before going abroad.

Competitive advantages often interact with potential gains from integrated global management. For example, high-technology firms tend to exploit their newest technologies via subsidiaries, while older products and processes are licensed to independent foreign producers. Likewise, some locational considerations cannot be separated from the benefits of a single global management structure. Much foreign direct investment is intended to enhance U.S. sales of goods imported from a firm's production facilities elsewhere, as with distribution and service facilities. This was true of Japan's early investments in the auto industry, which were related mainly to distribution and service rather than the local manufacture of vehicles. U.S. operations can also enhance exports by the parent to the host market by providing up-to-date market information when conditions are changing rapidly, thus keeping the parent in close touch with market trends.

Some advantages of multinational activity are associated with being multinational rather than with any specific host location. A global production network permits the firm to diversify risk and, more generally, increases its options when conditions are volatile. The risk-management motive helps to explain investments in the post-1973 era of volatile financial markets as well as the earlier U.S. foreign direct investments in extractive industries.

Enhanced opportunities for tax avoidance are a much-cited potential benefit of multinational operations. Through the use of advantageous transfer prices, firms are often able to increase global after-tax profits by reducing reported profits in higher-tax jurisdictions. This is a longtime practice of U.S.-based multinationals. Now the counterpart activity of foreign companies operating in the United States has begun to attract attention. Some officials charge that foreign corporations are benefiting from access to the U.S. market without paying their fair share of U.S. taxes.

Tax-law changes under the 1986 U.S. Tax Reform Act may have increased the profitability of U.S. investments for certain foreign multinationals. Although the reform raised the effective tax rate on most types of capital located in the United States, this increase was neutralized for foreign firms based in countries offering a tax credit for taxes paid to other governments (this applies to both Japan and the United Kingdom, the leading source countries for direct

investments in the United States). The tax increase thus raised the value to some foreign corporations of U.S. businesses relative to what those same assets were worth to domestic firms.⁷

The weak dollar

Exchange-rate movements are the most important determinant of ex-post rates of return on many types of internationally traded assets. Thus, anticipated *movements* in currency values should play a significant role in shaping international capital transactions. Currency *levels* may also be important, but mainly to the extent that they serve as a proxy for anticipated future movements toward a trend value such as purchasing power parity. This implies an essentially speculative motive, which should be more important for portfolio than for direct investments, since the latter involve a longer planning horizon. But even for direct investments, anticipated currency movements may well affect timing of flows.

As Table 1 shows, inward direct investment in the United States climbed steadily from 1985 to 1989 as the dollar fell from its 1985 peak. Some critics complain that the decline in the dollar allowed foreigners to buy U.S. assets at bargain prices.⁸ But the hypothesis that a weakening dollar produced the surge in inward investment leaves unexplained the substantial growth of U.S. direct investment abroad over the same period.

Other things equal, a lower dollar does make U.S. products a better buy in world markets. Is the same true for U.S. assets? If a U.S. asset (a factory or a hotel, for example) is seen as a claim to a fixed stream of future dollar-denominated profits, and if those profits will be converted back into the domestic currency of the investor at the same exchange rate, the level of the exchange rate does not affect the present discounted value of the investment. Neither a permanently strong nor a permanently weak dollar should affect the rate of investment.

If the profit stream is generated by an activity that requires imported inputs or that results in exports to other markets, the dollar value of the profits will not typically be independent of the exchange rate. However, the direction of the effect is ambiguous - some investments will become more profitable, others less so, as the dollar falls.⁹

In general, a weak dollar makes the United States more attractive as a *production* site. By lowering U.S. production costs relative to those in Europe or Japan, a fall in the dollar might shift locational preference for direct investors toward the United States. Even so, some advantage of integrated global management would still be required to make direct investment a profitable response to the new currency values. Otherwise U.S. firms would be better able

to exploit the locational advantage of lower production costs.¹⁰ Moreover, currency values are not the only determinant of profitability. During the U.S. recession of the early 1990s, a weak dollar has not been enough to bring in new investments. The new inflow has been quite small.

The role of import barriers

International trade theory predicts that restricting trade flows will stimulate compensating factor flows. If the United States limits imports of autos, for example, it seems almost self-evident that frustrated foreign suppliers ought to establish domestic production in the United States.¹¹ The U.S. auto industry and electronics industry seem to offer visible support for the proposition. Yet statistical analyses of Canadian and U.S. data have failed to confirm a systematic relationship between direct investment and protection.

The likely reason for the weak empirical findings is that protection creates a locational advantage by raising the cost of serving the market through trade. In some cases this locational advantage does promote foreign investment, but in others it affects mainly domestic entry and exit. When there is no firm-specific competitive advantage best exploited through integrated global management, domestic producers should be better able than subsidiaries of foreign companies to capture the benefits of local production.¹²

The conspicuous cases of autos and electronics, important though they are in their own right, may thus be exceptions to the general rule. In these industries, technological and managerial know-how are advantages that allow foreign producers to compete effectively with established U.S. firms. By contrast, the highly protected U.S. apparel and footwear industries have seen relatively little direct investment from abroad. For these low-technology industries, firm-specific advantages are apparently too small to offset the greater costs incurred by foreign investors.

Evidence at the country rather than the industry level also casts doubt on the role of protection as a strong magnet for inward direct investment. Among the less-developed countries, open export-oriented economies have been more successful than nations pursuing import-substitution strategies in attracting new investment. For U.S. outward investments, Canada, the United Kingdom, and Germany, all with relatively liberal trade regimes, have been the most important host countries.

The microeconomic analysis suggests that two trends stimulated the inflow of direct investments into the United States during the 1980s. The first and probably more important trend is the increase in the international competitiveness of companies based outside the United States. The second is the increase in factors that make locating in the United States a more profitable option for

those competitive foreign firms than alternative strategies like trade or licensing agreements. Confirming this microeconomic account is that, rather than being spread uniformly throughout U.S. business activities, the new manufacturing investments are clustered in the same industries where foreign firms have been outcompeting U.S. firms via trade.

The impact on U.S. capital and labor

Given that ownership of U.S. operations is basically a way for highly competitive foreign firms to enter the U.S. market, its most predictable effect is to reduce profits of firms already in that market. This is true both for U.S. firms and for foreign firms that have previously entered the market through exports or direct investment. However, the profits of firms that do not compete directly can also be affected. The new entrants' operations change demand for both outputs and for productive inputs. They also affect regional and national tax revenues and public expenditures. In the longer run, foreign ownership is likely even to affect the legal structure within which the industry operates, as new owners lobby for advantageous legislative and regulatory action.

An increase in employment is the benefit most eagerly sought by host regions, yet the actual impact of new foreign investment on employment and earnings is complex. Localities want foreign investments because they create "new jobs." But it is unlikely that overall demand for the product rises significantly as a consequence of new ownership. The new jobs therefore mainly replace others lost elsewhere, either at home or abroad, depending on whether the new output substitutes mainly for imports or for other domestic production. Moreover, the substitution of jobs will not be one for one if the investors' competitive advantage includes higher efficiency in production. Empirical evidence suggests that foreign owners in the United States pay roughly the same wages as domestic owners in the same industry but have higher output per worker.¹³ The number of jobs in the industry nationwide is thus likely to fall unless much of the new production replaces imports. Even if mainly imports are replaced, on average foreign-controlled producers use a higher percentage of imported intermediate inputs.¹⁴ This can mean job losses for workers in the domestic industries that produce these inputs. Working in the opposite direction is that foreign-based firms may, especially in the longer run, prove to be more adept than their U.S.-based rivals in exporting to markets elsewhere. If so, the United States would gain additional jobs at the expense of workers abroad.

Although the effect on labor is complex, at least wages and employment can be observed directly. This is not true in the case of technology. For less-developed nations, one strong motive for attracting foreign investment is the presumption that multinationals will provide a channel for transfer inward of advanced technology from abroad. The same hope is expressed by many U.S. policy makers and business people. The problem is that technology transfer is a two-way street.

Critics of a *laissez-faire* policy toward inward direct investment worry that some investments will serve as listening posts, facilitating the dissemination to foreign-controlled companies of proprietary U.S. technologies. The issue of potential loss of leading-edge technologies has been raised explicitly in many recent instances, including the attempted (friendly) takeover of Fairchild Semiconductor by Fujitsu in 1986 and the joint venture of McDonnell-Douglas with Taiwan Aerospace proposed in 1991. .

Foreign ownership in the U.S. auto industry

Although the highly visible auto industry is not typical of U.S. manufacturing overall, its situation illustrates vividly the complex interaction of import competition, foreign-controlled domestic production, and industry performance. In 1991, the Big Three auto makers racked up huge losses - the biggest in fact since the disastrous period a decade earlier that ended with imposition of voluntary export restraints by Japan. Now, however, import competition is no longer the key issue. Rather, weak overall demand for autos together, with steady growth of output from Japanese-owned "transplants," has left General Motors, Ford, and Chrysler with a diminished share of a shrinking total.

While forcing Japanese companies to produce cars in the United States for the U.S. market was an explicit goal of the restraints, the results have been far from satisfactory to those who sought protection. Instead of limiting the presence of Japanese producers in the U.S. market, the voluntary restraints greatly increased the profitability of their export sales. Soaring profits in turn helped to finance the new Japanese-controlled production subsidiaries that now enjoy a major share of U.S. production. By the end of 1991, Japanese-controlled factories accounted for about one of every six autos produced in North America. In the space of a decade, what had been competition from imports has become competition from new domestic producers.

The effect on employment is also different from what was anticipated by the United Auto Workers, the most important labor union for the industry. Although the transplants have, as expected, created new jobs, these were more than offset by layoffs at Big Three plants that continued throughout the 1980s. Moreover, many of the new jobs were in areas far from the hardest-hit labor markets in Michigan and the adjoining states. Also, many of the new workers are employed in non-union factories. The successful adaptation of Japanese companies to production in the United States has in fact required the United Auto Workers to reevaluate its own longstanding policies toward work rules, job rotation, and other aspects of labor-management relations.

The U.S. policy response

Given this complicated picture, it is no surprise that American policy makers have found it difficult to identify the national interest and to decide what to do about it. During the 1960s and 1970s, American policy toward direct investment reflected almost exclusively the nation's role as the major source country for outward direct investment. As the United States has become a leading host to inward investment, the U.S. policy process has responded to the changed circumstances, but with a significant lag. That lag is particularly evident in official U.S. positions for the Uruguay Round, the latest round of multilateral trade negotiations sponsored by the General Agreement on Tariffs and Trade (GATT).

Investment-related issues were included on the agenda for the Uruguay Round at the insistence of U.S.-based multinational firms and labor groups. However, U.S. priorities for the round were set at a time when the nation's policy concerns were still focused primarily on outward investments by American firms. Accordingly, complaints from U.S. business and labor had highlighted the presumed effects on U.S. employment, production, and profits of performance requirements imposed by a number of less-developed host countries and by Canada under its Foreign Investment Review Act.¹⁵

Ironically, U.S. efforts within the GATT started to bear fruit just when direct investments by European, Canadian, and Japanese firms in the United States had begun a period of rapid growth, and American worries had become more like those of other host countries. Even when the United States had emerged as the world's top host country in terms of the total value of inward direct investment and Congress was actively considering new policies to monitor and regulate the activities of foreign companies within its borders, U.S. negotiators continued to press for limits on the use of trade-related investment measures by host countries. In fact, many of the measures proposed in Washington violated the spirit of guidelines advocated concurrently by U.S. negotiators in Geneva; almost all the Congressional proposals conflicted with the fundamental principle of national treatment that has been central to U.S. policy toward foreign direct investment throughout the post-World War II period.¹⁶

What role for the United States?

The greatly increased extent of two-way foreign direct investment (and even of intraindustry investment, i.e., two-way flows within a given industry), has blurred the distinction, at least among industrial nations, between host and source countries. In the 1960s, the United States was the preeminent and indeed the quintessential source country. It was thus also the most conspicuous potential beneficiary of international limits on nationalistic policies of host countries. By the end of 1991, the United States remained a major source country as well as

the strongest voice for international action to regulate investment policies. Yet it had also become the world's most important host to direct investment, with all the new political pressures that entailed. Correspondingly, the European Community as well as Canada and Japan had gained a new stake in placing limits on host-country investment policies, and particularly those of the United States.

A key policy question on foreign investment for the United States in the 1990s is therefore analogous to the one raised by the national debate on trade policy a decade earlier, i.e., whether the United States is willing and able to champion global goals even when this requires some sacrifice of perceived national needs. Specifically, is the United States willing and able to continue its leadership role in combatting investment policies that achieve nationalistic objectives at the expense of global efficiency? Or will it instead join other host countries by adopting its own nationalistic policies?

Notes

- 1 In this paper I use the terms foreign ownership and foreign direct investment (FDI) interchangeably to refer to any ownership arrangement that allows a foreign-based firm to exercise a management role in the operation of U.S. business. The statistical criterion in the U.S. official data is that the foreign company must hold at least ten percent of the equity of the U.S. business.
- 2 After President George Bush's much-publicized trip to Japan in January 1992, a "Buy American" campaign revealed widespread public confusion over which autos were actually made in America. Several of the most popular Japanese-brand vehicles are now produced in U.S. factories; conversely, small imports from Japan and Korea often carry the name plates of the Big Three auto makers. As discussed below, U.S. production entails substantial use of imported parts. This is true for all producers, but the percentages are higher for most of the new Japanese-controlled factories.
- 3 During the 1992 presidential campaign, Paul Tsongas observed that the Democratic Party traditionally loves the employees but hates the employer.
- 4 In some cases, an ownership stake is purchased in exchange for proprietary technology, with no financial capital transferred.
- 5 On the development of the theory, see Kindleberger (1969) and Graham and Krugman (1991).
- 6 The three necessary conditions are elaborated by Dunning (1981 and earlier papers). Dunning uses this classification to explain the distribution of investment by home and host country and by industry.
- 7 Scholes and Wolfson (1988).
- 8 On the "fire sale" issue, see Graham and Krugman (1991).

- 9 Caves (1989). Another argument appeals to a wealth effect on firms facing imperfect capital markets. Other things equal, a fall in the dollar increases the wealth of foreign firms and thus allows them to outbid their domestic counterparts (Froot and Stein, 1989). However long-range corporate planning of investment expenditures in terms of the home currency would have a similar effect on observed dollar flows.
- 10 Given the large swings in key rates during the 1980s from apparent undervaluation to apparent overvaluation and back again, the explanation for recent increases in U.S. investments may lie less in the specific level of the exchange rate at the time of the investment than in the high probability of future large movements. Here global management plays a key role, increased costs in one location to be offset by reduced costs elsewhere and permitting some flexibility in shifting marginal production between locations on different sides of a major rate alignment.
- 11 Investments can also be the implicit price paid by foreign firms to avoid increased trade barriers. Bhagwati (1985) has coined the term *quid pro quo* investment to describe this link.
- 12 Local policies to attract new investment may also provide important locational advantages. Like market protection, such incentives are typically available to domestic as well as foreign firms.
- 13 For comparisons of U.S.-controlled and foreign-controlled U.S. companies, see Leonard and McCulloch (1991) and Graham and Krugman (1991).
- 14 On this point and the relationship between foreign ownership and trade performance more broadly, see Lipsey (1991).
- 15 Despite its own initiatives to curb such practices, the United States has been far from immune to their attraction. Moran and Pearson (1988) found that that nearly half of U.S. state governments offered investment incentives, prompting the authors' observation that although the United States has no local-content legislation, "it would be disingenuous to suggest that the pursuit by certain states of foreign-owned automobile plants has no impact on the country's trade flows."
- 16 The Exon-Florio provision of the Omnibus Trade and Competitiveness Act of 1988 provided presidential authority to block a foreign takeover deemed threatening to U.S. national security. By the time Exon-Florio lapsed in 1990, only one transaction had actually been stopped, although other potential takeovers may have been deterred (Graham and Krugman, 1991). A recent proposal would replace national treatment of inward investment with a reciprocity standard aimed at Japan. These legislative initiatives parallel the trend in the 1980s in U.S. trade policy.

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